Audit of City Treasurer In Rem Foreclosure Processes

MARTIN MATSON
City Comptroller

STACEY MAZMANIAN
Audit Manager

City of Milwaukee, Wisconsin

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Martin Matson
Comptroller

Glenn Steinbrecher, CPA
Deputy Comptroller

Aycha Sirvanci, CPA
Special Deputy Comptroller

Toni Biscobing
Special Deputy Comptroller

Office of the Comptroller

April 10, 2015

Honorable Tom Barrett, Mayor
The Members of the Common Council
City of Milwaukee
Milwaukee, WI 53202

Dear Mayor and Council Members:

The attached report summarizes the results of our audit of the City Treasurer's Office in rem foreclosure processes. The objectives of the audit were to: 1) assess the adequacy and effectiveness of internal controls within the department's in rem foreclosure filing processes; 2) determine whether the tax foreclosure activity is in compliance with Wisconsin Statutes, specifically parts of chapter 74, 75, and 985 related to property tax collection, tax sales, and publication of legal notices, respectively, that are within the scope of the audit; and 3) verify whether transactions are processed accurately and timely.

Between 2011 and 2014, the City acquired over 2,800 properties through in rem tax foreclosure. The Treasurer's Administration and Tax Enforcement Division prepares the documentation for filing foreclosure action with the Circuit Court, and prepares the final documents to close the file after the redemption and answer periods. The audit identified a number of internal controls within these processes and found the foreclosure activity was performed in compliance with relevant Wisconsin Statutes and City Ordinances. The controls are adequately designed and operating effectively; and transactions are processed accurately and timely. The audit does not make any recommendations. The report includes one audit observation related to the qualifications of newspapers for publishing legal notices.

Appreciation is expressed for the cooperation extended to the auditors by the staff of the City Treasurer's Office.

Sincerely,

Stacey Mazmanian, CIA, CGAP
Audit Manager

City Hall, Room 404, 200 E. Wells Street, Milwaukee, WI 53202 • Phone (414) 286-3321 • Fax (414) 286-3281
www.milwaukee.gov/comptroller

I. Audit Scope and Objectives

The audit examined the City Treasurer's processes performed to acquire properties through in rem tax foreclosure, encompassing the parts of the pre-foreclosure collections processes as necessary to determine adequacy of controls and compliance with state statutes (i.e., notice of issuance of tax certificate which is mailed during the first year of delinquency, and each year thereafter). Specifically, audit procedures covered the following functions of the City Treasurer's Office:

- Preparation of in rem filing documents,
- Notification of foreclosure action,
- Public notice of proceeding in rem to foreclose tax liens,
- Preparation of the judgment documents,
- Notification of proceeds,
- Administering applications for vacation of in rem judgment, and
- Processing write-off transactions.

The audit excluded property management activity performed by the Department of City Development after foreclosure judgment is received. The audit also excluded any parts of the tax foreclosure processes performed by the Comptroller's Office, the City Attorney's Office, and the Department of Neighborhood Services.

Audit methodology included developing an understanding of processes and controls for acquiring property through in rem tax foreclosure. The audit procedures developed to evaluate the processes and controls to meet the audit objectives included process walk-throughs, inspection of relevant control documentation, tests of controls, and detail testing. Procedures and tests performed included:

- Recalculating the penalty rate and the interest rate on delinquent general property taxes, special charges, special assessments, and special taxes included in the tax roll for collection to confirm the rates charged were in compliance with Wisconsin Statutes;
- Confirming the commencement of proceeding to foreclose the tax lien did not occur before one year after the date of the tax certificate;

- Verifying the list of tax liens filed with the circuit court was properly titled and contained the information required by Wisconsin Statutes;
- Confirming a copy of the petition and a description of the parcel was mailed by certified mail to the last known post office address of each owner and mortgagee of record;
- Confirming the public notice of in rem proceeding with the list of tax liens and petition was published for at least three days in a qualified newspaper;
- Verifying the redemption date was scheduled for at least eight weeks from the date of the first publication of the public notice of in rem proceeding;
- Confirming the City Treasurer notified the former owner, by certified mail, that the former owner may be entitled to a share of the proceeds of a future sale;
- Verifying applications to vacate judgment were processed in compliance with Milwaukee Code of Ordinances section 304-50; and
- Verifying write-off transactions were processed accurately.

Information obtained and reviewed included internal policies and procedures, certain sections of the City Charter and Code of Ordinances, certain sections of the Wisconsin Statutes, tax certificates, the list of tax liens filed with the circuit court, affidavit of verification, certified mail registers, affidavit of mailing, issues of the Daily Reporter, applications to vacate judgment and the accompanying written report to the City Clerk, and delinquent property tax bills and write-off transaction receipts. The audit focused on delinquent real property taxes eligible for foreclosure in 2014.

This audit was conducted in accordance with generally accepted government auditing standards. Those standards require that the audit obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objectives. Internal Audit believes that the evidence obtained provides a reasonable basis for the audit's findings and conclusions based on the audit objectives.

The objectives of the audit were to:

1. Assess the adequacy and effectiveness of internal controls around foreclosure management;

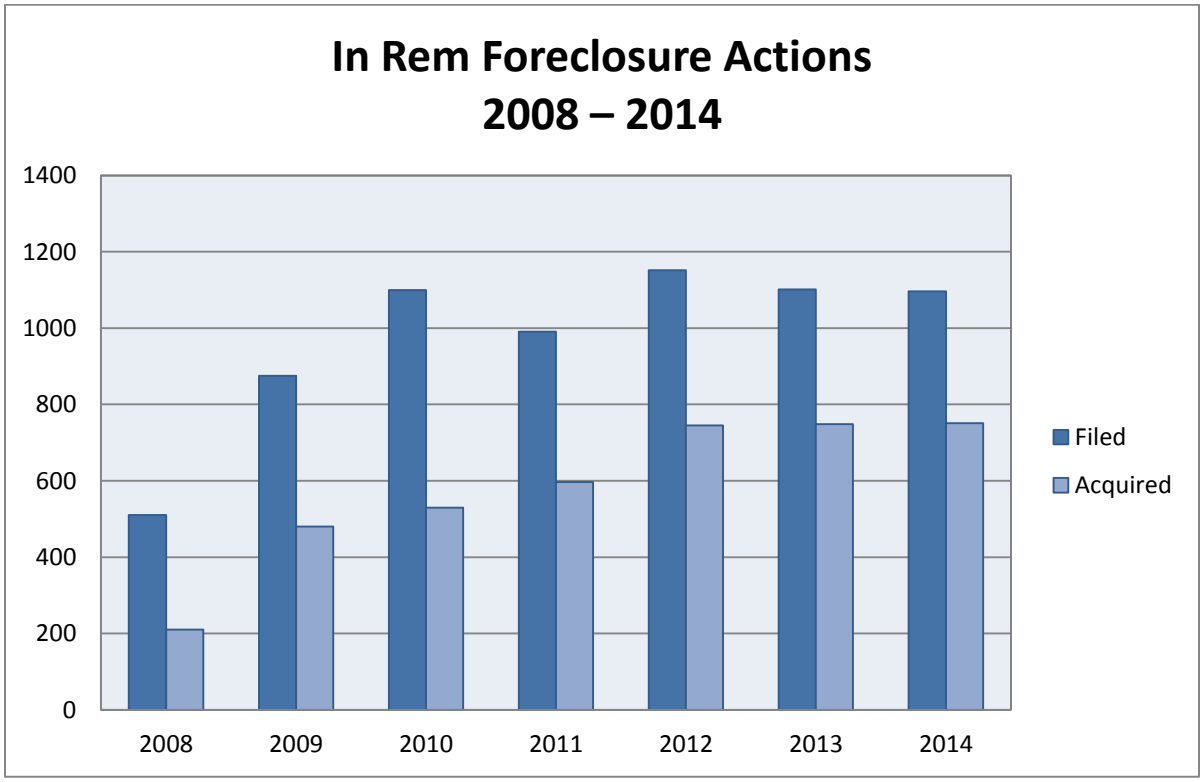
2. Determine whether the tax foreclosure activity is in compliance with Wisconsin Statutes, specifically parts of chapters 74, 75, and 985 related to property tax collection, tax sales, and publication of legal notices, respectively, that are within the scope of the audit; and
3. Verify whether foreclosure filings are processed accurately and timely.

II. Organization and Fiscal Impact

The City Treasurer receives and accounts for all monies paid to the City, makes disbursements vouchered for payment, invests City funds that are not needed to meet current expenditures, collects current property taxes and delinquencies, settles property tax collections on a prorated basis, and remits to each taxing jurisdiction their share of the monies collected.[1] This audit focused on the tax enforcement duties, specifically those related to in rem tax foreclosure.

The number of foreclosure filings and property acquisitions increased considerably in 2009 and has continued to increase every year since. In 2014, the City filed against 1,100 properties through in rem foreclosure; about 750 of those properties were ultimately acquired. Chart 1 shows historical data for filings and acquisitions since 2008.

Chart 1



The current tax collection period is in December and January of each year. To be considered a timely payment, the full tax payment, or the first installation must be received by the City

[1] 2015 Plan and Budget Summary

Treasurer on or before January 31. Any payments not received by January 31 are considered delinquent and subject to interest and penalty charges.

The Wisconsin Constitution Uniformity Clause prohibits granting preferential property tax treatment to specific property owners. Consequently, the City of Milwaukee cannot negotiate the tax amounts owed or waive interest and penalty charges. Due dates are also non-negotiable.

The Treasurer's Office utilizes a three-phase program for collecting delinquent real estate property taxes:

- In-house collection efforts,
- Use of a collection agency, and
- In rem[2] foreclosure.

Fifty to sixty percent of delinquent taxes are collected through in house collection efforts. What cannot be collected through internal processes is sent to the collection agency. Foreclosure is the third and final step. The Treasurer's Administration and Tax Enforcement Division prepares the foreclosure petition for the City Attorney to file in Circuit Court. Upon judgment after the redemption and answer period, the City takes ownership of the property in lieu of receiving the outstanding taxes.

Foreclosure of tax liens by action in rem is regulated by Wisconsin Statute 75.521. Noncompliance could cause a delay in the process or result in the foreclosure being void and the City losing the property. In rem tax foreclosure is a last resort and the City has opted to defer in rem foreclosure action for as long as allowed by state law. Former owners or other interested parties may even request the Common Council vacate the judgment for up to 90 days after the City acquires the property.[3]

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[2] In rem means an action is being taken against a property instead of a person (in personam). In rem literally translates to "against the thing." An in rem action to foreclose is a legal action to create a foreclosure sale. A foreclosed property is sold for fair market value, which may or may not be enough to cover the taxes due.

[3] As a condition of vacating the in rem foreclosure judgment, the petitioner must pay all outstanding fees and charges due before the Common Council meeting at which the petition will be acted upon. The property taxes due and all costs incurred by the City while the property was under DCD management must be paid in full within 30 days of the Common Council's approval. If the petitioner owns other City properties that are tax delinquent, the outstanding balances due on the other properties must also be paid in full, or a confirmed payment arrangement plan must be agreed upon and put in place (OverviewOfTheDelinquentGeneralRealEstateTaxCollectionProcess).

III. Audit Conclusions and Recommendations

The first objective of the audit was to assess the adequacy and effectiveness of internal controls around foreclosure management. The second objective was to determine whether the tax foreclosure activity is in compliance with Wisconsin Statutes, specifically parts of chapters 74, 75, and 985 related to property tax collection, tax sales, and publication of legal notices, respectively. Finally, the audit confirmed foreclosure filings are processed timely and accurately.

The audit identified a number of internal controls within the foreclosure management processes and found the foreclosure activity was performed in compliance with relevant Wisconsin Statutes and City Ordinances. The audit does not make any recommendations; controls are adequately designed and operating effectively, and transactions are processed accurately and timely. This report includes an observation relating to qualifications of newspapers for publication of legal notices. An observation may not constitute a recommendation, but should be taken under advisement. Additional details are provided in Section B below.

A. Internal Controls

The Treasurer's Office prepares the court documents, notifies the owners and interested parties of the foreclosure proceedings, publishes the public notices, sends out the notification of proceeds letters, administers applications to vacate judgment, and collects all the payments received during the redemption period, the answer period, and the 90-days after judgment for applications to vacate. These processes are performed in compliance with state and local laws, while being mindful of the inherent personal nature of foreclosures. Inaccurate or noncompliant foreclosure actions would increase legal burden and may weaken public trust. The audit identified a number of controls the Treasurer's Office has developed and implemented to reduce the likelihood of these risks.

The process for preparing the filing documents is fairly manual, with some clever automated workarounds built in for consistency. Data from the Automated Tax Collection System (ACTS) is exported into Microsoft Access databases which is then pulled into Word templates using mail merge commands. Other internal controls include:

- Documented policies and procedures;

- Restricted access to foreclosure files housed on the network;
- Copies of all documents are retained; and
- Interest and penalties are automatically calculated by the ACTS. Rates are based on those allowed by state statutes.

The above controls were tested as part of the audit and found to be operating effectively.

B. Compliance

Audit procedures also included testing to confirm compliance with certain sections of Wisconsin Statutes chapters 74 (Property Tax Collection), 75 (Land Sold for Taxes), 985 (Publication of Legal Notices, Public Newspapers, Fees), and Milwaukee Code of Ordinances chapter 304; where no specific controls were identified. The audit criteria applied for compliance testing is detailed in Appendix A. Testing results confirmed processes performed by the Office of the City Treasurer to foreclose tax liens by action in rem, including the processes leading up to and after the acquisition of the properties, are performed in compliance with the applicable state statutes and City ordinances. It should be noted that foreclosure actions are filed in the court by the City Attorney, and once acquired, City-owned properties are managed by the Department of City Development (DCD). Activities performed by the City Attorney and DCD were excluded from the scope of this audit.

Audit Observation: Qualifications of newspapers for publishing legal notices

Wis Stats 985.03 provides that a newspaper is qualified for the publication of legal notices when:

- The newspaper has been published regularly and continuously in the city where published for at least two of the five years immediately before the date of the notice publication, and has had a bona fide paid circulation:

    1. That has constituted fifty percent or more of its circulation; and,
    2. That has had actual subscribers at each publication of not less than 1,000 copies in first and second class cities.

- The newspaper is published at regular intervals and at least once a week, containing reports of happenings of recent occurrence of a varied character, such as political, social,

moral and religious subjects, designed to inform the general reader (this includes a daily newspaper published in a county having a population of 500,000 or more, devoted principally to business news and publishing of records, which has been designated by the courts of record of the county for publication of legal notices for a period of 6 months or more).

- The newspaper files a certificate with the county clerk stating that it qualifies under this section and stating its place of publication.

The publisher of the Daily Reporter provides a signed and notarized Proof of Publication to the City for every filing. The Proof of Publication is a notarized affidavit that states the Daily Reporter is a public newspaper of general circulation that fully complies with the laws of Wisconsin relating to the publication of legal notices.

The audit noted the Treasurer's Office does not perform any independent procedures to confirm the Daily Reporter meets the requirements for a qualified newspaper under Section 985.03 of Wisconsin Statutes. If notices are not published in a qualified newspaper, it could be construed as improper notice and the foreclosure would be void. The City of Milwaukee has a blanket contract with the Daily Reporter. The contract was not subject to competitive bidding as there is no other newspaper that publishes local official notices. A requirement to comply with Wisconsin Statutes relating to the publication of legal notices is not a stipulation of the contract.

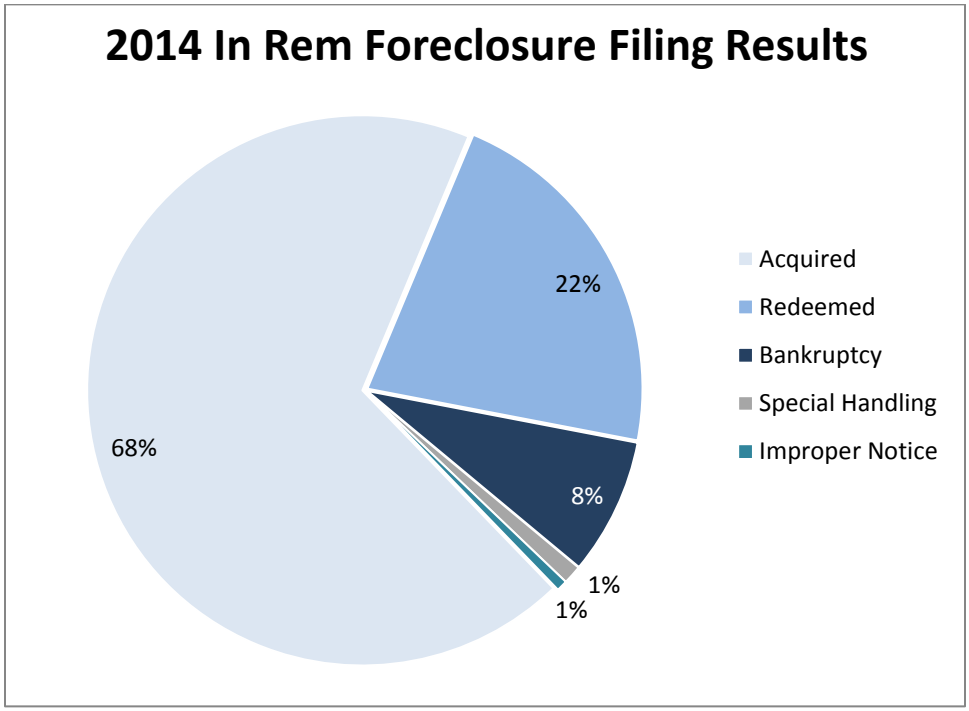
C. Accuracy and Timeliness

The audit focused on delinquent real property taxes eligible for foreclosure in 2014. Chart 2 shows the filing results for the year under review. The Treasurer's Office prepared five foreclosure filings with a total of 1,100 properties. Almost 70% of the parcels included in the filings were acquired (750). Over 200 properties were redeemed, meaning the former owner or other interested party paid all outstanding taxes and charges. Redeemed properties remain on the tax roll.

Transactions tested for accuracy and timeliness included interest and penalty rate calculations, account eligibility for foreclosure action, information in the filing and judgment documents,

applications to vacate judgment, and write-offs (2013). All transactions and activity tested as part of the audit were found to be accurate and timely.

Chart 2



Appendix A
Audit Criteria for Compliance Testing

1. Wisconsin Statutes

    a. Wis Stats §74.47(1) & (2) Interest and penalty on delinquent amounts.
        i. Interest. The interest rate on delinquent general property taxes, special charges, special assessments and special taxes included in the tax roll for collection is one percent per month or fraction of a month.
        ii. Penalty allowed. Up to one half of one percent per month or fraction of a month, in addition to the interest, on any delinquent general property taxes, special assessments, special charges and special taxes included in the tax roll.

    b. Wis Stats §74.57(2) Two years after the issuance of the tax certificate, the city may commence an action to foreclose the tax lien represented by the certificate under § 75.521.

    c. Wis Stats §75.36(2m) Notice, proceeds. Upon acquisition of a tax deed under this chapter, the treasurer shall notify the former owner, by certified mail sent to the former owner's mailing address on the tax bill, that the former owner may be entitled to a share of the proceeds of a future sale.

    d. Wis Stats §75.521(3)(a)1-4 Commencement of proceeding to foreclose tax lien.
        i. The treasurer may file with the clerk of the circuit court, a list of parcels of property affected by unpaid tax liens after one year elapses from the date of the tax certificate.
        ii. The parcels shall be numbered consecutively in the list. The list shall be known as the "List of Tax Liens of the City of Milwaukee Being Foreclosed by Proceeding in Rem (year), No. …." And shall bear the following caption:
            "State of Wisconsin
            Circuit Court
            Milwaukee County
            In the matter of the foreclosure of tax liens under section 75.521 Wisconsin Statutes by Milwaukee County, List of Tax Liens for (year), Number ….". The list shall contain as to each parcel, the following:
            1. A brief description.
            2. The name or names of the last owner or owners and mortgagee or mortgagees.

3. The amount of the principal sum of each tax lien with the date from which and the rate at which interest shall be computed.
4. A petition to the court for judgment vesting title to each of said parcels, as of the date of entry of judgment.

e. Wis Stats §75.521(3)(b) Such list of tax liens shall be verified by the affidavit of the treasurer and shall be posted in the treasurer's office.

f. Wis Stats §75.521(3)(c) A copy of the petition and so much of the list of tax liens as shall include the description of a particular parcel shall be mailed by certified mail, return receipt requested, by the treasurer to the last-known post-office address of each owner and mortgagee of record. An affidavit of the treasurer setting forth the names of the owners and mortgagees for whom a post office address has been ascertained, giving the addresses and stating that notice was mailed, giving the date of mailing, and stating that no present post office address was ascertainable for the other owners and mortgagees, shall be filed.

g. Wis Stats §75.521(6) Public notice of in rem proceeding. Upon the filing of the list of tax liens with the circuit court, the treasurer shall prepare a notice that such list of tax liens and petition has been so filed and a copy thereof posted in the office of the treasurer. The treasurer shall cause such notice, together with the list of tax liens and petition, to be published as a class 3 notice, under ch. 985. The notice shall insert a date at least 8 weeks from the date of the first publication of the notice fixed as the last day for redemption.

h. Wis Stats §985.03 Qualifications of newspapers.
   i. For at least 2 of the 5 years immediately before the date of the notice publication, the newspaper has been published regularly and continuously in the city where published, and has a paid circulation:
      1. That has constituted 50% or more of its circulation; and
      2. That has had actual subscribers at each publication of not less than 1,000 copies in first class cities.
   ii. A newspaper, under this chapter, is a publication that is published at regular intervals and at least once a week, containing reports of happenings of recent occurrence of a varied character, such as political, social, moral and religious subjects, designed to inform the general reader. This includes a daily newspaper published in a county having a population of 500,000 or more, devoted principally to business news and publishing of records.

iii. A newspaper in order to be eligible under this section shall file a certificate with the county clerk stating that it qualifies under this section and stating its place of publication.

i. Wis Stats §985.07(3) Class 3 notices. All notices designated as class 3 notices require 3 insertions.

2. Milwaukee Code of Ordinances

a. City Ordinance 304-38 City Penalty on Delinquent Taxes. In accordance with state statutes, the common council imposes a penalty of .5% per month, or fraction of a month, on any delinquent general property taxes, special assessments, special charges and special taxes included in the tax roll. This penalty is in addition to the interest.

b. Ch. 304-50 Vacation of In Rem Judgment. The city will reopen and vacate the city's in rem judgment only where:
   i. The former owner of record or any person having an interest of record has submitted a written request to the treasurer.
   ii. Not more than 90 days have elapsed from the date of in rem judgment.
   iii. The city has not accepted an offer to purchase the property.
   iv. The requestor has interest of record in the property.
   v. The written request identifies the property address, the tax key number, the applicant's name and mailing address and the applicant's interest in the property.
   vi. The requester paid the administrative costs of the various city departments.

Spencer Coggs
City Treasurer

James F. Klajbor
Deputy City Treasurer

OFFICE OF THE CITY TREASURER
Milwaukee, Wisconsin

April 2, 2015

To the Honorable
Mayor Tom Barrett and
Members of the Common Council
City of Milwaukee

Dear Mayor and Council Members:

This is written in response to the single audit observation found on page 8 in the *Audit of City Treasurer In Rem Foreclosure Processes* prepared by Audit Manager Ms. Stacey Mazmanian of the City Comptroller's Office, dated April 2015.

This office utilizes the *Daily Reporter* to fulfill its obligation to publish the requisite notice of each in rem tax foreclosure action under Wisconsin State Statute 75.521. As noted in the audit, this office does receive a Proof of Publication which is a notarized affidavit that states the *Daily Reporter* is a public newspaper of general circulation that fully complies with the laws of Wisconsin relating to the publication of legal notices, pursuant to Wisconsin State Statute 985.03.

However, the audit stated that this office did not perform any procedures to independently confirm that the *Daily Reporter* met the requirements set forth in Wisconsin State Statute 985.03. The *Daily Reporter* is utilized by <u>all</u> City agencies, departments, and offices under the terms of a City-wide blanket contract procured by the Department of Administration, Business Operations Division (DOA-BOD) for required public notices.

This office strongly holds that the DOA-BOD should be held responsible for independently confirming that the *Daily Reporter* meets the requirements set forth in Wisconsin State Statute 985.03 for public notices in lieu of the individual user departments doing so.

In addition, this office recommends that the DOA-BOD also include a requirement in the contract with the *Daily Reporter* that it complies with Wisconsin State Statutes relating to the publication of legal notices.

Respectfully submitted,

SPENCER COGGS
City Treasurer

MILWAUKEE
City Hall, Room 103 • 200 East Wells Street • Milwaukee, Wisconsin 53202
Telephone: (414) 286-2240 • FAX: (414) 286-3186 • TDD: (414) 286-2025
E-Mail: ctreas@milwaukee.gov • Web Page: http://www.milwaukee.gov/treasurer